

Republic of Iraq

2004 Budget

Minister of Finance
Minister of Planning

October 2003

(a) The following definitions are used in this Budget Paper:

- Budget year refers to 2004, while the forward years refer to 2005 and 2006, and the Budget period is 2004-6; and
- one billion is equal to one thousand million.

(b) Figures in tables and generally in the text have been rounded. Discrepancies in tables between totals and sums of components are due to rounding:

- estimates are in New Iraqi Dinar (NID);
- estimates are generally rounded to the nearest 100 million New Iraqi Dinar; and
- estimates midway between rounding points are rounded up.

(c) For the budget balance, a negative sign indicates a deficit while no sign indicates a surplus.

(d) The following notations are used:

NID	New Iraqi Dinar
-	Nil
na	not available
bn	Billion
\$m	\$ million

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Budget Overview

This Budget provides authority for the commitment and expenditure of money by the Interim Government of Iraq for 2004 and sets the fiscal framework for 2005 and 2006.

As a consequence of over two decades of neglect by the former regime, Iraq has immediate reconstruction and redevelopment needs well in excess of available revenues.

The Budget meets, to the extent possible with available revenues, the recurrent costs of the Iraqi government, some of the most pressing capital projects and around NID 940 billion (\$US 625 million) in urgent nation building programs.

Iraq will run a deficit in 2004 of NID 886.3 billion (\$US 590.9 million), financed by refunds of unspent Oil-for-Food funds. In 2005 and 2006, the budget is in balance (see Table 1).

Table 1: Budget Aggregates for 2003 to 2006

	2003(a) bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Revenues				
Oil	4,096.5	18,000.0	27,750.0	28,950.0
Customs Duty	-	450.0	525.0	-
Income Tax	-	45.0	120.0	240.0
Returns from State Owned Entities	337.5	562.5	142.5	150.0
User pays fees and charges	85.5	96.3	132.5	185.1
Other taxes and income	76.5	105.0	105.0	120.0
Total Revenues	4,596.0	19,258.8	28,775.0	29,645.1
Expenditures				
Operating Expenditure	7,362.3	19,026.7	21,119.2	21,463.8
Capital Projects	1,869.9	1,118.4	7,636.5	8,154.0
Total Expenditures	9,232.2	20,145.1	28,755.7	29,617.8
Budget Balance (Deficit)	4,636.2-	886.3-	19.3	27.3

(a) The 2003 Budget only covers July to December 2003.

In 2005 and 2006, revenue growth will permit Iraq to commit increased expenditures to much needed investment projects. These investment projects will grow to around NID 8 trillion (\$US 5.3 billion) in 2005 and 2006.

The Budget process identified very substantial reconstruction and redevelopment needs, nearly all of which are not able to be funded in the 2004 Budget. The Iraqi Governing Council, in conjunction with the Coalition Provisional Authority, is seeking the support of the international donor and investment community to meet these unmet needs.

Budget Financing

Consistent with responsible fiscal policy this Budget does not rely on increased borrowing or printing money. Rather, the Budget deficit of NID 886.3 billion (\$US 590.9 million) for 2004 will be financed from the return of unspent Oil-for-Food program funds.

Table 2 outlines the financing of Iraq's budgets for the coming years.

Table 2: Budget Financing for 2003 to 2006

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Opening Financial Capital				
Development Fund for Iraq	1,500.0	1,513.8	177.4	166.7
Vested Assets	1,350.0	-	-	-
Seized Assets	825.0	-	-	-
Total Opening Financial Capital	3,675.0	1,513.8	177.4	166.7
Plus: Capital Inflow				
Oil-for-Food Program Refunds	2,025.0	900.0	420.0	-
Transfer of Iraqi assets from abroad	450.0	-	-	-
Less: Capital Outflow				
Transfer to Central Bank Reserves	-	1,350.0	450.0	-
plus/less: Budget Surplus/deficit	4,636.2-	886.3-	19.3	27.3
Closing Financial Capital				
Development Fund for Iraq	1,513.8	177.4	166.7	194.0
Vested Assets	-	-	-	-
Seized Assets	-	-	-	-
Total Closing Financial Capital	1,513.8	177.4	166.7	194.0
Memorandum Item				
Cumulative Central Bank Reserves	450.0	1,800.0	2,250.0	2,250.0

The **Development Fund for Iraq** (DFI) was established by the United Nations Security Council Resolution 1483 to be administered by the CPA, in consultation with the interim Iraqi authority. Contributions to the DFI have included a \$US1 billion (NID 1.5 trillion) transfer from Iraq's Oil-for-Food program account, proceeds from oil export sales, and funds in other countries that belonged to the previous regime. These funds may only be used for humanitarian assistance, economic reconstruction, Iraqi civil administration and other purposes benefiting the Iraqi people.

Vested assets consisted of approximately \$1.7 billion (NID 2.55 trillion) in Iraqi funds that previously belonged to the former regime in Iraq were frozen in US bank accounts and vested by the President of the United States in a special account of the United States

Department of Treasury. These funds will be fully disbursed in paying salaries and pensions to Iraqi civil service workers and to fund other Iraq relief and reconstruction projects in 2003.

Seized Assets These funds consist of state owned or regime owned cash that was captured and safeguarded by Coalition Forces in Iraq. The authority for use of these funds was delegated to the CPA Administrator to use only to assist the Iraqi people and to support reconstruction of Iraq. All of these funds will be disbursed in 2003.

In addition to these funds, US Government appropriated funds are also being used to assist in the reconstruction of Iraq.

Relative to the 2003 Budget that was published in July, the 2004 Budget has reclassified US Government appropriated funds to being 'off budget' sources of finance. These appropriated funds however are noted below.

Iraq Relief and Reconstruction Fund (IRRF):	\$US 2.475 billion (NID 3.71 trillion)
Natural Resources Risk Remediation Fund (NRRRF):	\$US 0.502 billion (NID 753 billion)
Army Operations and Maintenance Funds for the New Iraqi Army transferred from the Iraq Freedom Fund:	\$US 0.101 billion (NID 151.5 billion)

These funds will be fully committed against 2003 requirements.

Economic and Fiscal Policy Overview

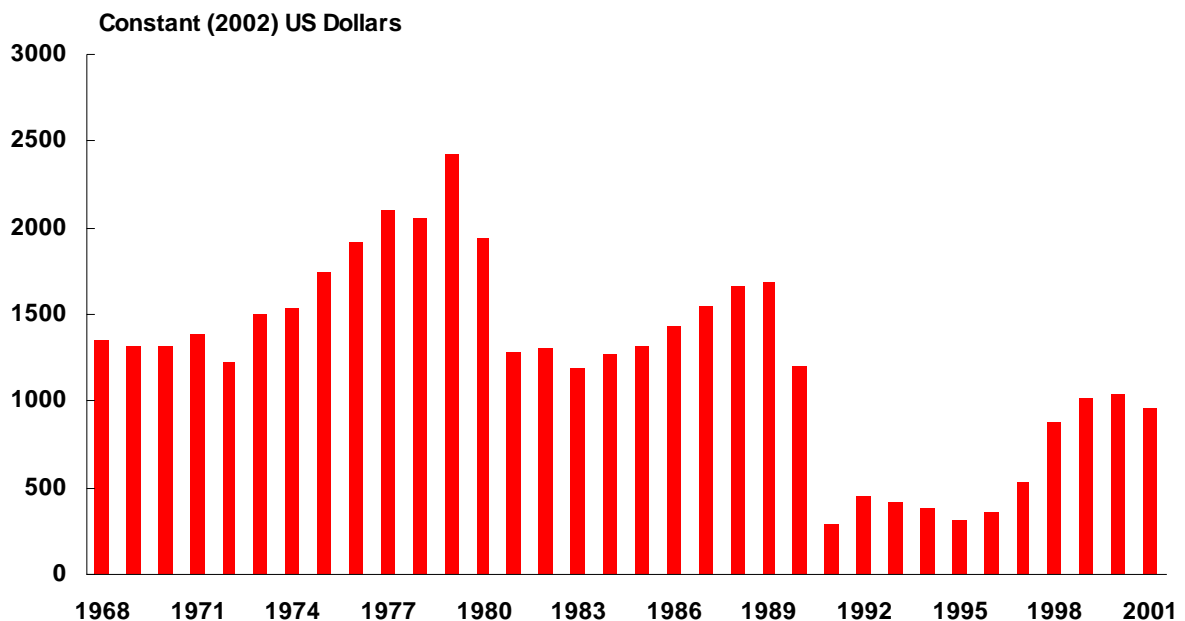
This section provides an overview of the fiscal and economic policy issues and challenges confronting Iraq. It starts with an analysis of Iraq's economy over the past three decades. An assessment of the current state of Iraq's economy and the challenges confronting it follows. This is followed by an outline of the fiscal and economic policy framework proposed to re-develop Iraq's economy to improve the living standards of the population, drawing on the lessons from other transition economies.

The decline of Iraq's economy

It is very difficult to get reliable economic and fiscal data for Iraq over the past two decades. Since 1979 the Iraqi national Budget was prepared in secret, and very closely held by the highest levels of the regime. Similarly, releasing core economic information about Iraq (Gross Domestic Product, unemployment and inflation rates) to the wrong hands carried the death penalty.

Nevertheless, the devastating economic effect of the previous regime's policies is undeniable. Saddam Hussein and his Ba'ath party presided over a very significant fall in living standards in Iraq, both in absolute and relative terms.

Chart 1: Iraqi per capita GDP: 1968-2001 (\$US 2002)



Source: Ministry of Planning, CPA estimates.

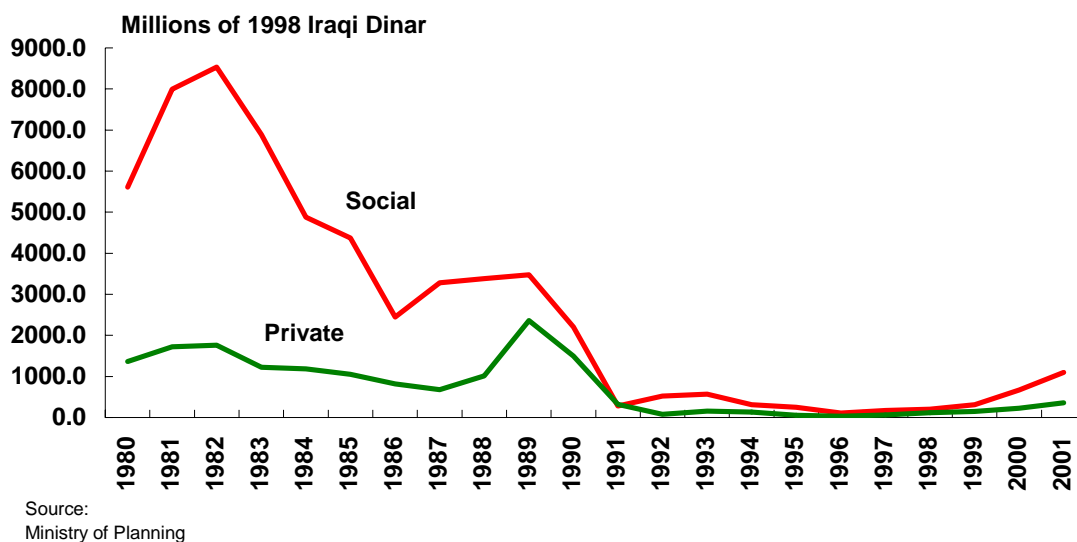
Thirty years ago, Iraq was an economic leader in the Arab world. Iraq had a strong workforce, modern infrastructure, and an effective public administration.

Today, while incomes of the rest of the world have gone forwards, per capita income in Iraq is a fraction of what it was 20 years ago (Chart 1).

The scale of this economic tragedy is difficult to overstate. The result is that Iraq today is an impoverished country, having once been a middle income country.

This decline in income co-incided with a collapse in infrastructure investment (Chart 2). This long term neglect of Iraq's vital infrastructure has left a legacy of a decrepit and fragile public infrastructure, and a capital stock a fraction of what it was two decades ago.

Chart 2: Gross Capital Formation in Iraq: 1980-2001



The economic legacy of Saddam Hussein

The source of Iraq's current problems stems from decades of economic mismanagement and corruption at the hands of Saddam Hussein and Iraq's Ba'ath party.

War, Opulence and Isolation

To some extent, this mismanagement is well known and broadly accepted. For example, the former regime:

- Started wars of aggression that cost untold Iraqi lives and tens of billions of dollars;

- Squandered Iraq's oil wealth on an opulent lifestyle for favoured officials of the previous regime, while ordinary Iraqis suffered a sustained decline in living standards; and
- Chose to isolate Iraq from the international community rather than dismantle its capacity for further military aggression against its neighbours and demonstrate that it had done so.

Some of the consequences of these policies are obvious.

The previous regime's wars and opulence diverted scarce resources away from social infrastructure and economic development. Its self-imposed isolation from the international business community has seen two decades of technological development pass it by, making state-owned enterprises increasingly inefficient. This is particularly evident in the crippled state of the banking and payments system.

Other consequences are less obvious.

The population policy of the previous regime was based on actively encouraging rapid growth in population to provide additional soldiers for its wars. However investment in education and housing declined, rather than increase in line with demand – in part reflecting the increased number of people seeking their share of Iraq's oil wealth.

In the first part of the 1990s, the previous regime's response to the international isolation it chose was to finance its spending by printing additional currency. The inevitable resultant hyperinflation created massive distortions throughout the economy, including the destruction of the real value of households saving deposits in the banks.

In the second part of the 1990s, the previous regime systematically and corruptly manipulated the humanitarian Oil-for-Food program instituted by Security Council resolution 986 and monitored by the United Nations.

The previous regime required that 10 per cent of the face value of contracts they submitted under the Oil-for-Food program be paid directly to the regime. These bribes were a key part in financing the palaces of the previous regime and maintaining and developing its military capability. In return, companies received inflated prices more than covering this additional cost.

In addition, a significant proportion of the goods imported under the Oil-for-Food program were on-sold by the State-owned enterprises at very significant discounts (over 50 per cent) in either local markets or smuggled out of the country to be sold in regional markets. The proceeds - much less than the oil exports used to purchase the goods - were then shared by the employees of the State-owned enterprises as 'profit' bonuses and the Iraqi budget (which in turn mainly funded the presidency and the military).

The result of this manipulation and corruption was that the humanitarian object of the Oil-for-Food program was undermined to a very significant degree. The extent of corruption under this program warrants further investigation.

State-Run Economy

Perhaps less obvious was the damage that the previous regime inflicted on Iraq through centralised command style economic policies.

The previous regime nationalised by force many industries from the 1970s. The consequence was a sustained reduction in the private sector's share of an already declining economy, as the private sector lost its incentive to save, invest and innovate.

The model of the State, rather than capital and product markets, determining the allocation of scarce financial capital has proven a failure across the world, as demonstrated by the collapse of the former Soviet Union. The experience of Iraq over the past two decades is yet another example, albeit among the most extreme, to add to this list.

Leaving aside the manner in which they were acquired, the enterprises run by the State have, almost without exception, been destroyers not creators of value, surviving only with subsidies from oil production.

Iraq's Economic Challenge

Iraq is a country with enormous economic potential. With sound policies, significant investments and assistance from international donors over the next several years, Iraq has the human and natural resources to return to the position of economic leadership it once held.

Fiscal and Economic Policy Approach

Iraq has significant reserves of natural resources. However ultimately, Iraq's economic future will depend on the adoption of sound fiscal and economic policies.

The objective of Iraq's fiscal and economic policy is to raise the living standards of all Iraqis as rapidly as possible through sustained economic growth.

Responsible fiscal policy is a key component of Iraq's economic strategy. The 2004 Budget was prepared on the basis that Iraq needs to demonstrate that it can operate with the resources available to it. The 2004 Budget does not rely on increased borrowing or printing money.

More generally, there are five core principles guiding Iraq's economic policy agenda:

1. Economic openness
2. Private sector development
3. International integration
4. Public sector transparency
5. A safety net for the poor.

Economic Openness

Economic openness is essential for markets to function properly, for business and job creation to occur, for ideas and entrepreneurship to flourish, and for Iraq to realise its full potential. The public sector has an important, but limited, role to play in everyday economic life.

Private Sector Development

The private sector, especially small and medium-sized companies that are often the most flexible and growth-oriented sector, will be strongly encouraged.

International Integration

Iraq is eager to fully rejoin the community of nations – practically and economically. Iraq will seek new and open trade relationships, financial links and other ties to the outside world to facilitate economic growth.

Public Sector Transparency

Iraq's institutions will be open to public scrutiny. Iraq's institutions will operate by clearly defined rules and will be held strictly accountable for their performance. This will help to reduce room for corruption and strengthen the confidence of investors and the Iraqi people alike.

A Safety Net for the Poor

Iraq must also help those suffering hardship now during this difficult economic transition. All Iraqis must share in Iraq's economic wealth. This will be done in a way that leaves people free to make their own choices but will also build a strong foundation for a market economy.

Lessons From Transition Economies

From the experience of other countries, we know that economic transitions are not easy and take time. The three decades of economic destruction wrought by the previous regime will not be undone overnight.

The history and stark facts of the twenty-odd transition economies during the last twenty years is that all of them suffered severe depressions and none of them started to grow in less than two years from the date they made the decision to change.

Iraq is in a much more difficult situation than other transitional economies since, unlike the transitional economies in the former Soviet Union, there is a significant security problem and a grossly inadequate infrastructure.

Given the years of neglect and war, the economy can't get into full gear unless the security problem is solved and the basic infrastructure which will facilitate economic development is repaired – electricity, water, sewage, transportation, communications and health.

The 2004 Iraqi Budget is the bare minimum necessary to keep Iraq going. It is nowhere near enough to kick-start the economy and create an enabling environment for future growth and prosperity.

Iraq will need international assistance to help it through this transition period, and enable it to take large strides back on the path to economic prosperity.

If started now, the security situation could be improved significantly within a year, the communications and electrical situation well on its way to being workable, and the water, sewage, health and transportation problems demonstrably on their way to success, completely changing the environment for investment.

These projects will of course significantly improve the employment situation and provide positive feedback on the security side.

Without this crucial investment there is little chance that the depressed private sector will recover in the short to medium term.

Iraq's Budget Process and Framework

Budget Process

The 2004 Budget process began in July 2004. Officials from the Ministries of Finance and Planning, in conjunction with the Coalition Provisional Authority (CPA), prepared and circulated guidance to Ministries, including “top line” provisional budget figures against which they needed to bid.

It included guidance on key assumptions to be used in the preparation of submissions, including a single exchange rate – 1500 NID to the US dollar.

In keeping with the principle of public sector transparency, this guidance was published on the internet at the same time it was provided to Ministries.

Ministries' budget submissions were received by the end of August. The Ministries of Finance and Planning conducted joint hearings in the first week of September in which each Ministry had the opportunity to explain and expound on the expenditure priorities they identified. These hearings were chaired by the Ministry of Finance and conducted in Arabic, with technical assistance provided by CPA officials.

The outcome of these hearings was then consolidated, and presented to the Governing Council and the CPA Administrator for approval.

Budget Coverage

Geographically, Iraq's budget was previously only for the Center and South of the country. This Budget covers all 18 governorates of Iraq, including the northern regions of Dohuk, Erbil and Suleymaniah. In the 2004 Budget, the northern regions of Iraq are treated as regional governments, with revenues flowing into the central Treasury consolidated revenue account and expenditures centrally funded by tied grants.

Budget Framework

Iraq's budget framework is characterized by a dichotomy between public entities that are 'on-budget' (all Ministries and their agencies that perform a public function) and 'off-budget' entities (also known as 'self-financing' entities).

All revenues of 'on-budget' entities are required to be put into consolidated revenue, controlled by the Ministry of Finance. Expenses of 'on-budget' entities are made against Budget appropriation lines.

Support for ‘off-budget’ entities is regarded as a transferred expenditure. Revenues of ‘off-budget’ entities are not required to be paid directly into consolidated revenue. Profits of State-owned enterprises are generally required to be transferred to the Ministry of Finance.

To avoid confusion, residual receipt of goods under the Oil-for-Food program are not recognised in the 2004 Budget.

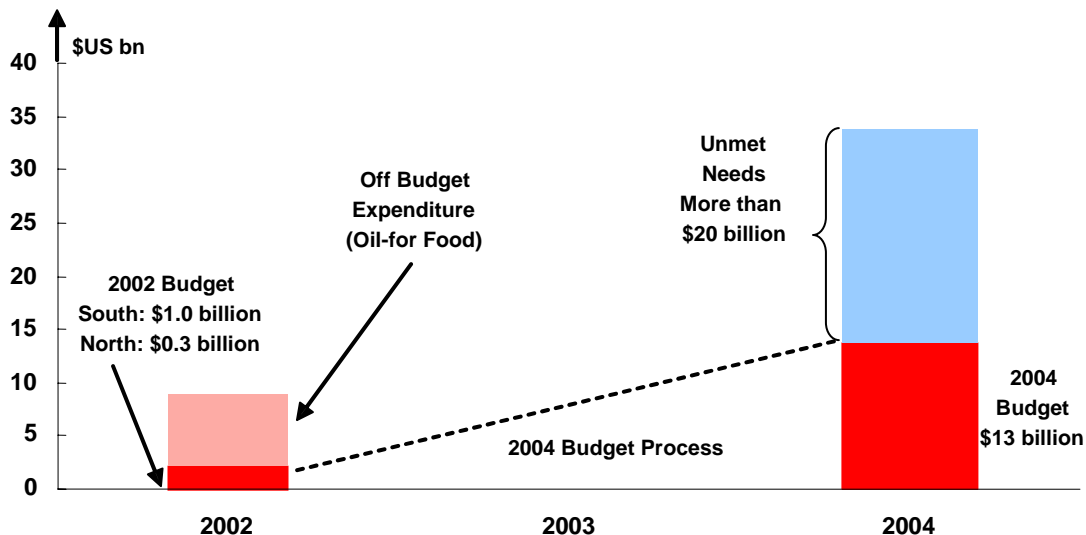
The Budget Challenge

A key challenge in preparing the 2004 Budget was the lack of a clear base on where funds were spent by the previous regime.

Of the appropriations ‘on-budget’, a variety of exchange rates were used, as a means of providing subsidies, and little detail exists on how or where military or Presidency appropriations were spent.

Further, the vast bulk of public expenditure under the previous regime was ‘off-budget’, reflecting goods received under the Oil-for-Food program. The manipulation of this program by the former regime presented a significant challenge in preparing the 2004 Budget.

Chart 3: Iraq’s budget challenge



Risks Surrounding the Estimates

The estimates of revenue and expenditure in this Budget incorporate the best information available at the time of publication. A range of factors may influence the actual budget outcome in future years.

The disclosure of these factors in this statement increases the transparency of the fiscal projections and ensures they remain 'on-balance' estimates.

Events that could affect fiscal outcomes include changes in economic and other parameters and matters not included in the fiscal forecasts because of uncertainty about their timing, magnitude and/or likelihood.

In particular, there are upside and downside risks to the oil price and export volume forecasts. Similarly, there is a possibility that tax revenues will be higher or lower than expected.

Should anticipated revenues be lower than expected, either expenditures would need to be reduced, or other revenue sources identified.

Revenues

An important element of the Budget fiscal strategy is the resumption of existing, and the creation of new, revenue sources. This is balanced against the impact on the development of the private sector. While the oil sector will provide the substantial majority of revenues in the near term, in 2004 Iraq will begin to diversify its revenue sources.

Total revenue for 2004 is forecast at NID 19.3 trillion (\$US 12.8 billion), increasing to NID 28.8 trillion (\$US 19.2 billion) in 2005 and nearly NID 30 trillion (\$US 19.8 billion) in 2006 as oil production increases (see Table 3).

Table 3: Revenues

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Oil Revenue	4,096.5	18,000.0	27,750.0	28,950.0
Reconstruction Levy	-	450.0	525.0	-
Personal Income Tax	-	15.0	45.0	90.0
Corporate Income Tax	-	30.0	75.0	150.0
Interest Income	76.5	15.0	-	-
Transfers from SOEs	337.5	562.5	142.5	150.0
User Pay Charges	85.5	96.3	132.5	185.1
Other Taxes and Charges	-	90.0	105.0	120.0
Total	4,596.0	19,258.8	28,775.0	29,645.1

Oil Revenue

The Budget assumes that the level of oil exports will rise over the forecast period to reach pre-war level of 2.5 million barrels per day in 2005 – rather than the production target of the end of 2004. It also assumes a decline in the oil price from current levels to \$US 21 per barrel over the Budget period. These assumptions reflect the need for Budget revenues to prudently balance risks.

	2004	2005	2006
Oil Revenue (NID bn)	18,000	27,750	28,950
Oil Exports (mb/d)	1.6	2.4	2.5
Oil Price (\$US)	21	21	21

Reconstruction Levy

A 5 per cent reconstruction levy will be levied on all goods, except humanitarian goods, imported into Iraq from 1 January 2004. The revenues from the Reconstruction levy shall

be used only to assist the Iraqi people and support the reconstruction of Iraq. It shall expire on 1 January 2006.

NID billion	2004	2005	2006
Reconstruction Levy	450	525	-

Personal Income Tax

From 1 January 2004, personal income tax will recommence, with a maximum rate of 15 per cent. It will be levied on the income of individuals, as defined under existing Iraqi income tax law. This lower rate, compared to the 75 per cent top rate that existed previously, will encourage compliance and reward effort.

NID billion	2004	2005	2006
Personal Income Tax	15	45	90

Company Income Tax

From 1 January 2004, company income tax will recommence at a flat rate of 15 per cent. It will be levied on the income of companies, including on the profits of foreign companies operating in Iraq.

NID billion	2004	2005	2006
Company Income Tax	30	75	150

Interest Income

The funds invested in the Development Fund for Iraq earn interest income.

NID billion	2004	2005	2006
Interest Income	15	-	-

Transfers from State Owned Enterprises (SOEs)

The following transfers are expected from SOEs in the forward estimates period.

Table 4: Revenue from State Owned Enterprises

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Central Bank of Iraq	-	75.0	90.0	105.0
Shopping Centers Company	-	75.0	7.5	-
Automobiles Company	-	150.0	7.5	-
Construction Materials Company	-	150.0	7.5	-
Agriculture Supplies Company	135.0	105.0	7.5	-
Al-Rasheed Hotel	7.5	7.5	22.5	45.0
Other enterprises	195.0	-	-	-
Total	337.5	562.5	142.5	150.0

Transfers are only expected from several of the nearly two hundred State Owned Enterprises (SOEs) in 2004. The bulk of the transfers anticipated in 2004 reflect the proceeds from the resale of goods imported under the Oil-for-Food program by companies overseen by the Ministries of Trade and Agriculture. The transfer from the Central Bank of Iraq reflects interest earned on Treasury notes less operating expenses, approved capital projects and some retained earnings.

User Pay Charges

One of the general principles underpinning this Budget is that Iraqis must contribute to the recovery of their economy. This includes paying for services used – at least to the extent this was done under the previous regime. By 2004 user pay arrangements will be re-implemented for:

- Vehicle registration;
- Other fees from emergency services;
- Passport Fees;
- Higher Education Course Fees;
- Court Fees; and
- Social Security Rental Income.

The revenue expected from these charges is displayed in the table below.

Table 5: Revenues from User Charges

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Passport Fees	-	0.8	0.8	0.8
Pharmaceutical scrip charge	15.00	30.0	37.5	45.0
Entry Fees to Cultural Institutions	0.15	0.8	0.8	0.8
Consultancy Charges	-	0.2	0.3	0.5
Sale of Statistical Publications	-	0.2	0.2	0.2
Court Fees	3.00	7.5	7.5	7.5
Social Security Rental Income	1.50	3.0	3.0	3.0
Vehicle Registration	-	30.0	45.0	60.0
Higher Education Course Fees	1.50	1.5	7.5	30.0
Other fees from emergency services	-	7.5	15.0	22.5
Flight overpass fees	7.50	15.0	15.0	15.0
Other fees and charges	56.85	-	-	-
Total	85.5	96.3	132.5	185.1

The structure of each of these fee arrangements will be reviewed by the responsible Minister, in consultation with the Minister of Finance, to assess its adequacy relative to the service provided. The details of this review for each of these fees and charges will be published no later than 31 December 2003.

In addition, there are several new fees and charges applicable in 2004:

- Flight overpass fees
- Pharmaceutical scrip charge (for non-exempt)
- Entry Fees to Cultural Institutions
- Consultancy Charges
- Sale of Statistical Publications

Flight overpass fees are charges for the use of Iraqi airspace by commercial airlines. A pharmaceutical scrip charge of NID 1500 per scrip will apply to help defray the large cost of pharmaceuticals. Exemptions will apply to this charge where its application would result in significant hardship. Entry fees will be charged at cultural institutions such as Baghdad Museum. The Ministry of Planning will charge for consultancy services and statistical publications provided to commercial interests (domestic and foreign) investigating investing in Iraq.

There are also some significant examples of other user pay arrangements in place that do not appear as budget revenue. For example, electricity charges are paid to State Owned Enterprises monitored by the Electricity Commission, rather than directly into consolidated revenue. Similarly, municipal water rates and charges are paid to the municipality directly.

Other Taxes

Several other taxes will be raised in 2004. These are outlined in the table below.

Table 6: Other Taxes

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Excise Tax	-	15.0	15.0	15.0
Hotel and Restaurant Service Tax	-	7.5	7.5	7.5
Land Tax	-	15.0	30.0	45.0
Other	-	52.5	52.5	52.5
Total	-	90.0	105.0	120.0

A 15 per cent excise tax will apply to alcohol and tobacco products and other items to be determined. Collection of the 10 per cent tax on 4 and 5 star hotel accommodation and restaurants and the real estate transfer tax resumed on 19 September 2003. A range of other smaller existing taxes will continue to be collected. It includes taxes collected by regional governments.

In order to fund an indigenous effort to search for and recover funds stolen from Iraq under the previous regime, a luxury tax of ten per cent will be placed on the profits of businesses delivering remote television access.

Budget Expenditures

This Budget provides authority for around NID 20 trillion (\$US 13.4 billion) in expenditure in 2004, increasing to NID 28.8 trillion (\$US 19.2 billion) in 2005 and NID 29.6 trillion (\$US 19.7 billion) in 2006, in line with increased revenues.

Table 7: Expenditure Aggregates

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Expenditures				
Operating Expenditure	7,362.3	19,026.7	21,119.2	21,463.8
Capital Projects	1,869.9	1,118.4	7,636.5	8,154.0
Total Expenditures	9,232.2	20,145.1	28,755.7	29,617.8

Expenditure information is presented in several different forms. First, operating expenditure and capital projects are presented for each Ministry and Statutory Authority, along with employment levels and staffing costs.

Operating expenditures are then broken down into the eight headings of the existing Iraqi budget system: staffing expenditures, service requirements, goods requirements, asset maintenance, capital expenditures, transferred expenditures, foreign obligations and staff and retirement rewards.

However, this presentation does not provide satisfactory guidance on what is being achieved by this spending. To correct for this gap, operating expenditures are also broken down into major initiatives in the Budget, along with normal ministry operating expenses.

Capital projects funded by the budget are listed, along with their estimated cost in 2004 and total project cost.

Finally, for each Ministry and statutory authority a summary of all expenditure items is presented.

Expenditure Summary by Ministry

Table 8 provides a summary of operating expenditure, capital projects and total expenditure approved in the 2004 Budget by Ministry and Statutory Authority.

Table 8	2004			2005			2006		
	Operating bn NID	Capital bn NID	Total bn NID	Operating bn NID	Capital bn NID	Total bn NID	Operating bn NID	Capital bn NID	Total bn NID
Agriculture	35.4	17.7	53.2	42.2	75.0	117.2	45.5	75.0	120.5
Communications	1.8	7.5	9.3	6.3	225.0	231.3	6.3	225.0	231.3
Culture	12.3	1.5	13.8	9.3	22.5	31.8	9.3	22.5	31.8
Displacement and Migration	0.9	1.5	2.4	0.9	7.5	8.4	0.9	15.0	15.9
Education	805.9	10.0	815.9	806.2	30.0	836.2	806.2	30.0	836.2
Electricity Commission	2.2	-	2.2	2.2	2,250.0	2,252.2	2.2	2,475.0	2,477.2
Environment	0.9	1.5	2.4	0.9	30.0	30.9	0.9	60.0	60.9
Finance	15,683.8	132.9	15,816.7	17,441.4	240.0	17,681.4	17,545.4	240.0	17,785.4
Foreign Affairs	57.6	9.0	66.6	56.9	15.0	71.9	56.9	15.0	71.9
Governing Council	9.6	-	9.6	12.0	-	12.0	15.0	-	15.0
Health	1,345.5	75.0	1,420.5	1,592.9	150.0	1,742.9	1,790.5	150.0	1,940.5
Higher Education	171.1	12.0	183.1	171.1	7.5	178.6	171.1	7.5	178.6
Housing	55.2	200.1	255.3	46.7	450.0	496.7	46.7	450.0	496.7
Human Rights	0.9	1.5	2.4	0.9	7.5	8.4	0.9	15.0	15.9
Industry and Minerals	12.0	-	12.0	9.0	1.5	10.5	9.0	1.5	10.5
Interior	187.3	-	187.3	200.0	150.0	350.0	215.0	150.0	365.0
Justice	144.6	63.3	207.9	134.4	150.0	284.4	134.4	150.0	284.4
Labour and Social Affairs	49.2	3.1	52.3	52.2	7.5	59.7	67.2	7.5	74.7
Municipalities and Public Works	60.0	249.0	309.0	84.5	727.5	812.0	84.5	975.0	1,059.5
Oil	2.7	-	2.7	1.9	1,500.0	1,501.9	1.9	1,500.0	1,501.9
Planning	45.0	22.5	67.5	54.9	-	54.9	61.6	-	61.6
Science and Technology	28.6	7.7	36.4	31.0	15.0	46.0	31.0	15.0	46.0
Trade	10.8	4.5	15.3	6.3	-	6.3	6.3	-	6.3
Transport	34.2	93.0	127.2	8.1	750.0	758.1	8.1	750.0	758.1
Water Resources	25.2	192.3	217.5	29.3	750.0	779.3	29.3	750.0	779.3
Youth and Sport	18.2	4.2	22.4	18.2	75.0	93.2	18.2	75.0	93.2
Statutory Authorities									
Board of Supreme Audit	4.1	0.5	4.5	3.8	-	3.8	3.8	-	3.8
Central Organisation for Standards	2.7	-	2.7	1.7	-	1.7	1.7	-	1.7
Awqaf (Religious Endowments)	2.1	8.1	10.2	2.3	-	2.3	2.3	-	2.3
Iraqi Media Network	2.2	-	2.2	2.2	-	2.2	2.2	-	2.2
New Iraqi Army	34.8	-	34.8	109.8	-	109.8	109.8	-	109.8
Unallocated	180.0	-	180.0	180.0	-	180.0	180.0	-	180.0
Total	19,026.7	1,118.4	20,145.1	21,119.2	7,636.5	28,755.7	21,463.8	8,154.0	29,617.8

Staffing Levels and Expenditure Summary by Ministry

This table provides a summary of the number of employees on the direct Government payroll by Ministry. An allocation of salaries has been provided to each Ministry to meet salary costs for these employees, using the interim four tier salary scale. The new 13 tier salary scale will increase the overall public sector wage bill. The budget allocation to fund this increase is only transferred to a Ministry when the proposed aggregate plan for allocating all of the Ministry's staff into the new tiers has been approved.

Table 9: Ministry Staffing Levels

	2004 Employees	2004 bn NID
Agriculture	8,166	19.7
Communications	174	0.3
Culture	3,213	5.1
Displacement and Migration	34	0.1
Education	324,532	655.9
Electricity Commission	846	1.4
Environment	34	0.1
Finance	6,633	14.4
Foreign Affairs	1,410	2.7
Health	105,481	220.5
Higher Education	50,055	107.3
Housing	16,409	30.2
Human Rights	34	0.1
Industry and Minerals	584	1.3
Interior	65,105	155.0
Justice	21,433	44.1
Labour and Social Affairs	5,413	11.7
Municipalities and Public Works	22,874	39.5
Oil	770	1.9
Planning	1,050	2.4
Science and Technology	10,041	16.0
Trade	1,419	3.0
Transport	1,888	4.1
Water Resources	6,958	14.3
Youth and Sport	2,427	3.2
Statutory Authorities		
Board of Supreme Audit	1,216	3.0
Central Organisation for Standards	500	1.0
New Iraqi Army	26,500	34.8
Iraqi Media Network	1,322	2.2
Governing Council	125	1.2
Centrally Funded Employees	353,578	1,762.5
Total	1,047,718	3,159.0

Operating Expenditure Summary by Input

This table provides a summary of operating expenditure broken down into the eight headings of the existing Iraqi budget system.

Table 10: Operating Expenditure Summary by Input

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Staff Expenditures	1,467.6	3,159.0	3,153.0	3,148.5
Service Requirements	277.2	544.8	544.2	584.0
Goods Requirements	419.7	1,101.1	1,354.0	1,528.9
Assets Maintenance	99.4	154.4	193.0	204.1
Capital Expenditures	154.1	159.4	179.3	192.8
Transferred Expenditures	4,173.1	11,182.8	12,406.2	12,223.7
Foreign Obligations	205.7	925.2	1,414.3	1,631.8
Salaries & Retirement rewards	565.5	1,800.0	1,875.0	1,950.0
Total Budget Inputs	7,362.3	19,026.7	21,119.2	21,463.8

Capital expenditures are regarded as operating expenditures if they represent the regular purchase of capital items necessary for the operation of a ministry, rather than representing a capital project or investment. New vehicle expenditures, for example, are recorded under this expenditure line.

Transferred expenditures include, amongst other things, the cost of the public distribution system and support for State Owned Enterprises.

The **Foreign obligations** category includes the war reparations to Kuwait required under Security Council resolution 1483 (discussed further below).

Operating Expenditure Summary by Output

Table 11 below provides a summary of operating expenditure by program initiatives. A brief description of each item follows.

Table 11: Operating Expenditure Summary by Output

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
Public Distribution System	-	5,250.0	7,350.0	7,350.0
Oil product imports	2,287.5	-	-	-
Normal Ministry Operating Expenditure	869.2	2,192.7	2,353.4	2,430.5
Contingency Reserve	-	1,125.0	1,500.0	1,500.0
Local/Regional Government Grants	294.0	1,117.5	1,117.5	1,117.5
Reserve for New Salary Scale	-	1,065.0	1,065.0	1,065.0
Regional Development Projects	340.5	1,116.0	450.0	450.0
Nation Building Projects	466.5	937.5	75.0	75.0
Pharmaceuticals	-	930.0	1,125.0	1,275.0
Kuwait War Reparations	205.5	900.0	1,380.0	1,447.5
Support for SOEs	558.0	750.0	675.0	600.0
Economic Restructuring Programs	160.5	750.0	750.0	750.0
Centrally funded salaries	1,467.0	697.5	697.5	697.5
Pensions and other Transfer Payments	225.0	675.0	750.0	825.0
Stipends to Demobilised Military	180.0	375.0	375.0	375.0
Agricultural Subsidies	-	300.0	300.0	300.0
Interest on Foreign Debt	-	-	300.0	300.0
Interest on Treasury Notes	-	210.0	210.0	210.0
Payment System Fees	-	135.0	135.0	135.0
Oil Export Production Fee	-	109.5	146.0	182.5
Consultancies	-	75.0	75.0	75.0
Haj subsidies	-	56.3	56.3	56.3
New Office for Landmine Removal	-	30.0	37.5	45.0
On the job training initiative	-	7.5	9.0	15.0
Recovery of Iraqi Assets from Abroad	-	5.4	-	-
Office of Foreign Litigation	-	5.3	-	-
Iba Agricultural Research Institute	-	3.0	3.0	3.0
Privatisation Consultants	-	3.0	-	-
Economic Policy Consultancy	-	3.0	3.0	3.0
Transition Management Assistance	-	3.0	-	-
Other Measures	308.5	199.6	181.0	181.0
Total Operating Expenditures	7,362.3	19,026.7	21,119.2	21,463.8

Public Distribution System

A central element of the Oil-for-Food program under Security Council Resolution 986 was the monthly provision of a ration of food to each Iraqi citizen in return for a nominal

fee. This ration represents the principal income of many Iraqi households. The estimated full year total cost of this program is NID 7.4 trillion. A reduced level of funding is necessary in 2004, reflecting the residual provision of food items under the Oil-for-Food program.

This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Public Distribution System	-	5,250	7,350	7,350

Normal Ministry Operating Expenses

Ministries require a level of funding to meet the normal (or base case) operating expenses (including salaries – except in 2003, where they were centrally financed).

Estimated cost (bn NID)	2003	2004	2005	2006
Normal Ministry Operating Expenses	869.2	2,192.7	2,353.4	2,430.5

Contingency Reserve

Given the uncertainty surrounding Iraq's situation, it is prudent to set aside a contingency reserve to cover the level of currently unidentified needs likely expected to arise over the Budget period. This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Contingency Reserve	-	1,125	1,500	1,500

Local and Regional Government Grants

Local and Regional governments provide services direct to their communities. Grants will be provided to these governments to supplement, not replace, their traditional financing sources - fees and charges for the services provided. This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Local/Regional Government Grants	294.0	1,117.5	1,117.5	1,117.5

Reserve for New Salary Scale

A new thirteen tier salary scale takes effect in October 2003. This reserve reflects the estimated additional cost of the new salary scale. The amount allocated to Ministries for salary expenses in this Budget reflect the previous four tier scale. As each Ministry has its allocations across the thirteen tiers approved, the additional cost will be transferred from this reserve to the Ministry's budget appropriation. This amount is included under salary expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Reserve for New Salary Scale	-	1,065	1,065	1,065

Nation Building Projects

With the fall of the previous regime, Iraq is in the transition to becoming a free and democratic society. This transition process requires many of the traditional democratic institutions and structures to be built, or at least significantly reconstructed. This measure provides funding of around NID 938 billion in 2004 and NID 75 billion in 2005 and 2006 for nation and institution building projects.

The projects that are expected to be funded under this measure are listed below. The Ministers of Finance and Planning have joint responsibility for assessing these proposals for submission to the Governing Council. This amount is included under transferred expenditures.

Table 12: Nation Building Projects

	2003 bn NID	2004 bn NID	2005 bn NID	2006 bn NID
National Census	-	150.0	-	-
Elections Assistance	-	75.0	-	-
Constitutional Development	-	45.0	-	-
Civil Society and Community Dvmt	-	30.0	-	-
WMD Scientist Retention	-	90.0	30.0	30.0
Legal claims/debt negotiation	-	15.0	-	-
Modernize banking system	-	30.0	15.0	15.0
Tax administration modernization	-	15.0	15.0	15.0
Stock Exchange modernization	-	7.5	-	-
Economic indices development	-	22.5	-	-
Labour force survey development	-	22.5	-	-
Other projects	466.5	435.0	15.0	15.0
Total Nation Building Projects	466.5	937.5	75.0	75.0

Kuwait War Reparations

United Nations Security Council resolution 1483 requires Iraq to pay 5 per cent of gross oil export revenues to meet reparation claims from the first Gulf war. This amount is included under foreign obligations.

Estimated cost (bn NID)	2003	2004	2005	2006
Kuwait War Reparations	205.5	900.0	1,380.0	1,447.5

Support for State Owned Enterprises (SOEs)

Iraq's State Owned Enterprises (SOEs) employ nearly 500,000 people. From 1 January 2004, salaries of SOEs employees will no longer be centrally funded directly from the Budget, but will need to be paid from SOEs revenues. With the greater consumer choice and lower prices associated with open borders many of these enterprises will be unprofitable as currently structured.

This budget provides NID 750 billion in 2004 in support for SOEs to enable them to resume and maintain operations as options for their future are assessed – it does not allow for significant reconstruction of destroyed facilities or significant new investment. Lesser amounts are set aside for 2005 and 2006 reflecting both an expected improvement in the profitability of these enterprises and the expectation that some less profitable enterprises would be closed.

This support has yet to be allocated to each SOE, as sufficient information is not yet available. Through their responsible monitoring Ministry, SOEs will apply to the Ministry of Finance for access to this support on a case by case basis as information on their needs becomes clearer. Updated lists of allocations to individual SOEs will be published at regular intervals.

This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Support for SOEs	-	750	675	600

Economic Restructuring Programs

The transition of Iraq's economy from centrally managed to one driven by market forces will involve significant restructuring of the economy. Economic restructuring programs are necessary to assist this transition process. Payments to workers made redundant through the closure or restructuring of State Owned Enterprises will reduce the hardship associated with this necessary but difficult process. Similarly training programs will assist in providing a closer match of the skills of the workforce with the changing demands of the labour market. This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Economic Restructuring Programs	160.5	750	750	750

Pensions and Other Transfer Payments

There is a range of pension and transfer payments in Iraq, including: pensions to retired public servants, military and their dependents; 'private' pension arrangements previously financed through the social security fund, and the 'family social bonus' paid to those in greatest need. The number of beneficiaries is expected to increase over the Budget period, as previous restrictions (eg, caps) are lifted. This amount is included under salaries and retirement rewards.

Estimated cost (bn NID)	2003	2004	2005	2006
Pensions and Other Transfer Payments	225	675	750	825

Stipends to Demobilised Military

With the dissolution of the old Iraqi Army, the Coalition Provisional Authority decided to pay, for an indefinite period, stipends to the demobilised military. A future Iraqi government will need to decide whether or not to continue paying these stipends. This amount is included under salaries and retirement rewards.

Estimated cost (bn NID)	2003	2004	2005	2006
Stipends to Demobilized Military	180	375	375	375

Agricultural Subsidies

Iraq's agricultural sector has a long history of state support and control. On the one hand this has involved the subsidized provision of agricultural inputs, while on the other hand price controls discouraged and distorted the pattern of agricultural production. The strategy in this Budget has two pillars – increasing agricultural output prices to market prices and delivering subsidies in a more efficient manner. This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Agricultural Subsidies	-	300	300	300

Interest on Treasury Notes

Iraq has around NID 3.5 trillion in Treasury notes on issue, with a coupon of 6 per cent per annum. The vast majority of these notes are held by the Central Bank of Iraq and the State owned commercial banks. Meeting the interest obligations on these notes will cost NID 210 billion per annum. This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Interest on Treasury notes	-	210	210	210

Interest on Foreign Debt

Iraq has very substantial levels of foreign debt. Security Council resolution 1483 provides a moratorium on interest and principal repayments until the end of 2004. The level of interest and principal payments on foreign debt beyond 2004 is a matter for future negotiations. In this budget, NID 300 billion is set aside for interest payments in 2005 and 2006. This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Interest on Foreign debt	-	-	300	300

Payment System Fees

The execution of this budget requires the movement and payment of significant amounts of currency. In 2003 many of these services have been provided by Coalition forces. In 2004, these services will need to be purchased by the Government of Iraq – usually, but not necessarily by SOEs (in particular the banks). The budget sets aside NID 135 billion per annum for fees and charges associated with payment system services provided to the Government. The amount paid for particular services is a matter for competitive commercial negotiations. This amount is included under service expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Payment System Fees	-	135	135	135

Oil Export Production Fee

Gross oil export revenue is recognized directly on the budget, in accordance with Security Council resolution 1483. It follows that expenses associated with the production of oil exports also need to be funded through the budget. This budget provides for NID 200 per barrel of oil exported to be paid to companies monitored by the Ministry of Oil. This amount is included under transferred expenditures.

Estimated cost (bn NID)	2003	2004	2005	2006
Oil Export Prod'n Fee	-	109.5	146	182.5

Consultancies

Iraq's Ministries will be confronted with a range of new issues and challenges over the period ahead, outside their recent institutional experience and expertise. To meet this challenge, Ministries will need to engage independent external consultants to advise on these issues and more generally to assist in building institutional capacity.

The range and type of these issues is not yet known with certainty, so it is not yet possible to allocate these amounts by Ministry and/or project. Rather, this funding provides a capped general allocation of NID 75 billion per annum that Ministries can apply to the Minister of Finance for access on a case by case basis as needs emerge. The Minister of Finance will publish details on consultancies approved at regular intervals. This amount is included under service requirements.

Estimated cost (bn NID)	2003	2004	2005	2006
Consultancies	-	75	75	75

Economic Policy Consultancy

The Minister of Finance will engage independent consultants to advise him on a range of economic policy issues. This amount is included under service requirements.

Estimated cost (bn NID)	2003	2004	2005	2006
Economic Policy Consultancy	-	3	3	3